

LETTER OPINION
94-L-206

August 11, 1994

Mr. Kent Reiersen
Williston City Attorney
P.O. Box 1366
Williston, ND 58802-1366

Dear Mr. Reiersen:

Thank you for your letter asking whether a city may invest general fund surplus funds in United States Treasury bills or notes where the securities are held in "street name" by an investment broker.

N.D.C.C. ? 21-06-07 provides that political subdivisions, including cities, may "invest surpluses in their general fund, or surpluses in any special or temporary fund, in bonds, treasury bills and notes or other securities which are a direct obligation of the treasury of the United States or of an instrumentality thereof." An obligation is "direct" when it operates by an immediate connection or relation, instead of operating through a medium. Black's Law Dictionary 459 (6th ed. 1990).

The determination of whether an obligation is a direct obligation refers to the remedy provided by law for enforcing the obligation rather than to the character and limits of the obligation itself. Rouse v. Wooten, 53 S.E. 430 (N.C. 1906). Thus, an obligation is direct when it is not conducted via a medium and when its enforcement can be made directly by the obligee against the obligor.

A security is held in "street name" when it is held in the name of a broker instead of the customer's name. This may occur when the securities have been bought on margin or when the customer wishes the security to be held by the broker. Black's Law Dictionary 1421 (6th ed. 1990).

"This practice of street name ownership consists of registering securities in a name other than that of the beneficial owner . . . a bank or brokerage house will function as owner of record on behalf of

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individual or institutional investors." Blum v. Bank Atlantic Financial Corp., 925 F.2d 1357, 1359 n.3 (11th Cir. 1991). In such an arrangement the broker is commonly known as the owner of record, registered owner, or legal owner; the investor is commonly called the beneficial owner or equitable owner. Id.; Berger v. Berger, 592 A.2d 321 (N.J. Super. Ch. Div. 1991).

Consequently, when a security is held in "street name" by a broker, the United States Treasury or an instrumentality thereof does not know the identity of the actual investor who supplies funds with which to buy the security, but deals with, and regards the security as held by, the broker. The direct or primary obligation of the United States Treasury is therefore to the broker as the holder of record, rather than to the investor as the beneficial owner. Accordingly, the investor here would look first to the broker-dealer or its guarantor or insurer in any action to enforce payment of the investment obligation.¹

Even though the broker is a participant in the Securities Investor Protection Corporation (SIPC) pursuant to the Securities Investor Protection Act of 1970 (15 U.S.C. ? 78aaa, et seq.), and may even have additional insurance to protect investors, the "street name" system of holding investment securities is not the one contemplated by N.D.C.C. ? 21-06-07. In any event, participation in SIPC or the existence of insurance is irrelevant to whether a security is a direct obligation within the meaning of that provision.

Because the wording of N.D.C.C. ? 21-06-07 is clear, its letter may not be disregarded (N.D.C.C. ? 1-02-05). It is my opinion, therefore, that a North Dakota city may not invest surpluses in its general or special funds in Treasury bills, notes, or bonds purchased through an investment broker where the

¹But cf. Berger v. Berger, 592 A.2d at 324-26 (beneficial owners of stock, who were not the record owners, could assert rights under state law to seek appraisal and dissolution of corporation).

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securities are held in "street name" by the broker.

Sincerely,

Heidi Heitkamp
ATTORNEY GENERAL

rel/pg
cc: Wayne Hokenson, Political Subdivisions Audit
Director, State Auditor's Office